In The

Supreme Court of the United States

October Term, 1939.

No.

HAROLD H. MOORE, Bankrupt,

Petitioner,

v.

LEONARD HORTON, Trustee in Bankruptcy,

Respondent.

BRIEF IN SUPPORT OF PETITION.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals for the Sixth Circuit is reported in *110 F. (2d) 189, 42 A. B. R. 485,* and is printed in the Record, pages 46-49. The opinion of the District Court for the Eastern District of Michigan is not officially reported but is printed in the Record, pages 34-39.

JURISDICTION.

Jurisdiction is claimed under the Act of February 13, 1925, as amended *(28 U. S. C. A. 347, 350)*. This application is made within three months after the motion for rehearing was denied in the Circuit Court of Appeals.

STATEMENT OF THE CASE.

The statement of facts in the foregoing petition (ante, page 2), in the interest of brevity, is not repeated. The will of the petitioner's father is printed in full in the Record, pages 8-12. Its pertinent provisions may be summarized in this way:

All of the estate (except for certain specific bequests) was willed to trustees to manage, collect, invest, etc. (R. 9), and to dispose of principal and income as follows: (A) To pay the income to the widow during her lifetime (R. 10). (We omit reference to the provision for an annuity to petitioner payable out of income, since this controversy only relates to the trust principal.) (B) To turn over to the widow so much of the principal as she might require for her support, etc., and the trustees might deem proper (R. 10). (C) To turn over half of anything remaining in the trust to the petitioner, if he should be living when the widow died (R. 10). (D) To turn over such half to others, if the petitioner should not survive the widow (R. 10-11). (E) To turn over the other half of the estate to the petitioner's sister. This case does not concern that portion of the estate.

This will was admitted to probate in 1928 (R. 6, 14). The petitioner was adjudicated bankrupt in 1936 (R. 1, 2, 6, 34), the creditors being chiefly the receivers of closed banks (R. 22-23). The petitioner was discharged in bankruptcy in 1937 (R. 1). The widow died in 1938 (R. 34). The Referee ruled that the bankrupt's expectancy was an asset available to the creditors (R. 14, 19). The District Court reversed the Referee's ruling (R. 34-39). The Circuit Court of Appeals reversed the District Court's order (R. 45). The bankrupt seeks a review in this court.

SPECIFICATION OF ERRORS.

1. The court erred in holding that the bankrupt's future contingent interest in the trust vested in the trustee in bankruptcy.

2. The court erred in holding that under the Michigan law the bankrupt's interest in the trust was an interest which he could have transferred.

3. The court erred in holding that under the Michigan law the bankrupt's interest, in so much of the trust as related to personal property, was an interest which he could have transferred.

4. The court erred in refusing to give to local statutes (Mich. C. L. 1929, Sec. 12955, 12982 Stat. Ann. 26.35, 26.66) the construction put upon them by the local courts.

5. The court erred in holding that the bankrupt's interest in the trust was "property" within the meaning of Section 70a (5) of the Bankruptcy Act, 11 U. S. C. A. 110a (5).

ARGUMENT.

We contend (I) that the questions here involved are of public importance; (II) that the Circuit Court of Appeals has failed to follow the decisions of the local courts on a question of local property law and the construction of local statutes which are common to many states; and (III) that in holding this bankrupt's expectancy to be "property" within the meaning of the Bankruptcy Act, the lower court decided a Federal question contrary to the decisions of this court and of the other Circuit Courts of Appeals.

I.

The importance of the questions involved.

The present state of the bankruptcy law with reference to expectant interests not subject to *in praesenti* transfer is described in a recent treatise (*3 Simes on Future Interests, Sec. 738)* as follows:

> "The decisions on this point have been conflicting. The Circuit Courts of Appeals in two circuits have held that such interests do not pass to the Trustee in Bankruptcy. One of these decisions, involving a Maryland estate, is inconsistent with a decision of a Federal District Court of Maryland and with a dictum of the Maryland Supreme Court. In accord with the view that the interests under discussion do not pass to the Trustee in Bankruptcy is also a decision of the Federal District Court of Vermont. To the

effect that a contingent interest transferable by estoppel, release, or 'in equity' does pass to the Trustee in Bankruptcy, is the decision of the Circuit Court of Appeals for the Seventh Circuit. That case involved Illinois property and is inconsistent with the decisions of the Illinois courts on the point, and also with a number of decisions by other state courts."

While there are differences in the local law, these differences do not account for the conflicting interpretations which the United States Courts have put on an Act of Congress. And insofar as construction of state statutes is involved in the present case, it is to be noted that many other jurisdictions have statutes similar to Mich. C. L. 1929, Sec. 12955, Stat. Ann. 26.35 (alienation of future estates in land), such as Arizona (Rev. Code 1928, Sec. 2760), California (Civil Code, Sec. 699), Delaware (Rev. Code 1935, Sec. 3698), District of Columbia (Code 1929, Title 25, Sec. 275), Georgia (Code 1933, Sec. 29-103), Idaho (Civil Code 1932, Sec. 54-109), Minnesota (Mason St. 1927, Sec. 8065), Montana (Rev. Codes 1935, Sec. 6695), New York (Real Property Law, Sec. 59), North Dakota (Comp. Laws 1913, Sec. 5277), South Dakota (Comp. Laws 1929, Sec. 284), Wisconsin (Stat. 1939, Sec. 230.35).

Other jurisdictions also have statutes similar to Mich. C. L. 1929, Sec. 12982, Stat. Ann. 26.66 (the *cestui* takes neither legal nor equitable estate), such as California (Civil Code, Sec. 863), Minnesota (St. 1927, Sec. 8095), Montana (Rev. Codes 1935, Sec. 6790), New York (Real Property Law, Sec. 100), North Dakota (Comp. Laws 1913, Sec. 5373), Oklahoma (St. 1931, Sec. 11829), South Dakota (Comp. Laws 1929, Sec. 380), Wisconsin (St. 1939, Sec. 231.16). A declaration by the Circuit Court of Appeals as to the meaning of these statutes is therefore of more than local importance.

Trust expectancies of this sort are becoming more common, due in part to income and estate taxes. All the courts have agreed that if such contingencies must be transferred to the Trustee in Bankruptcy, and offered by him at public sale, he can realize little or nothing, though the bankrupt may lose a great deal. The Circuit Court of Appeals for the Eighth Circuit has said *(Jones v. Harrison, 7 F. (2d) 461 at 465)*:

> "The result would be small benefit to the creditors, and disastrous loss to the beneficiary. Such considerations as these give an impressive force to the placing of the property in trust, as evidencing the intent of the testator to put it beyond the reach of such sacrifice and waste."

The legal status of such expectancies ought to be put beyond question and made uniform, and their sacrifice at a bankruptcy sale ought to be prevented unless the Act of Congress plainly requires it.

The questions here involved are of bankruptcy law, on which the lower courts are divided; and of the construction of statutes which are local, but common to many states. We urge that their importance is such as to merit an early review in this court.

II.

The Circuit Court of Appeals has decided a question of local law in a manner contrary to the determination of the local courts.

The bankrupt's interest was that of a *cestui que trust;* whether he would enjoy any part of the estate in possession was contingent, both on his being alive at an uncertain future date, and on the trustees not exercising their discretionary right of consuming the trust corpus by advancing it to the life tenant (R. 10). By the local law of Michigan such a *cestui* takes no estate, either vested or contingent, and has only a chose in action:

> *C. L. 1929, Sec. 12982, Stat. Ann. 26.66;*
> *Palms v. Palms, 68 Mich. 355 at 380, 36 N. W. 419 at 439;*
> *Culbertson v. Witbeck, 127 U. S. 326 at 334-335, 32 L. Ed. 134 at 137.*

By the local law such a *cestui's* interest cannot be assigned:

> *Hunt v. Hunt, 124 Mich. 502, 83 N. W. 371;*
> *Weaver v. Van Akin, 71 Mich. 69, 38 N. W. 677.*

and it cannot be reached by his creditors:

> *Allen v. Merrill, 223 Mich. 467, 194 N. W. 131;*
> *Lee v. Enos, 97 Mich. 276, 56 N. W. 550.*

Michigan is one of the states in which a valid spendthrift trust may be created even though alienation is not expressly prohibited in the trust instrument:

> *Hackley v. Littell, 150 Mich. 106, 113 N. W. 787;*

Perry v. Avery, 148 Mich. 211, 111 N. W. 746;
Fleming v. Wood, 147 Mich. 513, 111 N. W. 80;
Cummings v. Corey, 58 Mich. 494, 25 N. W. 481.

The District Court found as a fact that the settlor's intention was such as to make this a spendthrift trust (R. 38) and this finding is now absolute, since the Trustee in Bankruptcy appealed to the Circuit Court of Appeals solely on a question of law (R. 41):

Carter v. Powell (C. C. A. 5, 1939), 104 F. (2d) 428.

The Circuit Court of Appeals based its decision (R. 49) upon a Michigan statute (C. L. 1929, Sec. 12955, Stat. Ann. 26.35) providing that expectant estates in land are descendible, devisable, and alienable. It failed to consider certain decisions of the Supreme Court of Michigan. These decisions announce, as a rule of property, that where the will bespeaks no different intention "it is a condition precedent to the remainderman taking any vested interest in such a contingent remainder that he survive the life tenant," and have refused to apply the statute in cases like the present one, because there is no "vested interest in the contingent remainder."

In re Coots, 253 Mich. 208, 234 N. W. 141;
Hadley v. Henderson, 214 Mich. 157, 183 N. W. 75.

This rule the State Legislature changed in 1931 by passing a statute permitting the transfer of such interests; but the statute only affects estates created thereafter, and cannot apply here:

Act No. 211, Public Acts of 1931, Stat. Ann. 26.47;
Stevens v. Wildey, 281 Mich. 377, 275 N. W. 179.

For a great many years we have had in Michigan the following statute (C. L. 1929, Sec. 12982, Stat. Ann. 26.66) which the Circuit Court of Appeals seems not to have considered:

> "Every express trust * * * shall vest the whole estate in the trustees in law and in equity, subject only to the execution of the trust; and the person for whose benefit the trust was created shall take no estate or interest in the lands, but may enforce the performance of the trust in equity."

Taking together this statute, and the fact that the testamentary trustees could have diverted the trust corpus before it reached the bankrupt, and that the bankrupt's right of inheritance was in any case contingent on an event which might never happen, we come within the rule stated in *16 A. L. R. 561:*

> "Where the beneficiary has no title, legal or equitable in the property, and no control over the trust, as where his rights rest absolutely in the discretion of the trustees, the property is not subject to the control of creditors, and the Trustee in Bankruptcy has no right therein."

This statement of the law is sustained by decisions of numerous state courts in cases where Trustees in Bankruptcy resorted to plenary suits in the local courts:

> *Brown v. Lumbert, 221 Mass. 419, 108 N. E. 1079;*
> *Robertson v. Schard, 142 Iowa 500, 119 N. W. 529;*
> *Peck v. Chatfield, 24 Ohio App. 176, 156 N. E. 459;*
> *Luttgen v. Tiffany, 37 R. I. 416, 93 Atl. 182;*
> *Bristol v. Atwater, 50 Conn. 402.*

and by decisions of Federal courts in bankruptcy:

> *In re Martin (C. C. A. 6, 1931), 47 F. (2d) 498;*

Suskin & Berry v. Rumley (C. C. A. 4, 1930). 37 F. (2d) 304;
Jones v. Harrison (C. C. A. 8, 1925), 7 F. (2d) 461;
Allen v. Tate (C. C. A. 8, 1925), 6 F. (2d) 139;
In re Wetmore (C. C. A. 3, 1901), 108 F. 520;
In re Hoadley (S. D. N. Y., 1900), 101 F. 233.

Because of the above statute, the beneficiary under a trust has no interest which is in the nature of real estate. Note *Hunt v. Hunt, 124 Mich. 502, 83 N. W. 371,* and *Weaver v. VanAkin, 71 Mich. 69, 38 N. W. 677,* where the point is stressed. The Circuit Court of Appeals cited a statute authorizing the alienation of interests in land, and construed it to apply to the *cestui's* interest, something which is not land. Upon this foundation it reversed the decision of the United States District Court sitting in Michigan. If everything else were left out of the case, we believe that this line of procedure is so illogical as to fully justify a review of the case in this court.

And furthermore, even if some basis could be found for treating as real estate the *cestui's* interest in a Michigan real estate trust, there is in this case the further fact that this trust was in part a trust of personal property. The theory of the lower court should have required the division of this interest into two parts, since Michigan has no statute relating to the alienation of future estates in personal property. At common law the interest of this bankrupt in the personal property is inalienable:

3 Thompson on Real Property, Sec. 2161;
Gray, Rule Against Perpetuities (3d Edition), page 81;
Roberts, Transfer of Future Interests, 30 Mich. Law Review 349 at 352-355.

We submit that insofar as this case is governed by the local law of Michigan, that law is correctly stated by the District Court in its opinion (R. 34-39).

III.

In holding the bankrupt's expectancy to be "property" within the purview of the Bankruptcy Act, the lower court decided a Federal question contrary to the decision of this court and of other Circuit Courts of Appeals.

Section 70a (5) of the Bankruptcy Act (11 U. S. C. A. 110a) vests the Trustee with the bankrupt's "property." It is for the Federal Courts to say what is meant by "property"; the question does not depend on the local law at all:

Board of Trade v. Johnson, 264 U. S. 1 at 10, 68 L. Ed. 533 at 536;
Page v. Edmunds, 187 U. S. 596, 47 L. Ed. 318.

Where, as here, it depends on the discretion of the testamentary trustees whether the bankrupt ever gets any of the principal, the bankrupt's expectancy is too uncertain to be classed as property, and does not pass to the trustee in bankruptcy:

Nichols v. Eaton, 1 Otto 716, 23 L. Ed. 254;
In re Martin (C. C. A. 6, 1931), 47 F. (2d) 498;
Suskin & Berry v. Rumley (C. C. A. 4, 1930), 37 F. (2d) 304;
Jones v. Harrison (C. C. A. 8, 1925), 7 F. (2d) 461;

Allen v. Tate (C. C. A. 8, 1925), 6 F. (2d) 139;
In re Harper (C. C. A. 2, 1907), 155 F. 105;
In re Wetmore (C. C. A. 3, 1901), 108 F. 520;
In re Hoadley (S. D. N. Y.), 1900, 101 F. 233.

In the same way the Federal Courts have consistently held that the word "property," as used in Section 70a (5) of the Bankruptcy Act, does not include the heir's expectancy of inheritance from his ancestor, or the devisee's expectancy of inheritance from a testator still living, regardless of the fact that by the local law such expectancy may be classed as a property right subject to alienation, and notwithstanding that the ancestor or testator may have become incapable of altering the succession:

In re Baker (C. C. A. 6, 1926), 13 F. (2d) 707;
Bank of Elberton v. Swift (C. C. A. 5, 1920), 268 F. 305;
In re Lage, 19 F. (2d) 153;
In re Hall, 16 F. Supp. 18;
In re Meiberg, 1 F. Supp. 892.

As a practical proposition of fact, this bankrupt's possibility of inheriting any of the trust principal was far less definite than is the possibility of inheritance possessed by a legatee under mutual and reciprocal wills which have become irrevocable. If the latter is not to be offered to the public at a bankruptcy sale, neither should the former be.

The precedents cited in the opinion of the lower court as requiring a different conclusion, will be found on examination to be not inconsistent with the above statements. Thus, *McArthur v. Scott, 113 U. S. 340, 28 L. Ed. 1015,* is not a bankruptcy case, but has to do with the construction of a will disposing of real estate in Ohio. *Comegys v. Vasse, 1 Pet. 193, 7 L. Ed. 108,* is not a bankruptcy

case, and deals with the assignability of personal injury claims for settlement under the provisions of an early treaty with Spain. *Pollack v. Meyer Bros. Drug Company (C. C. A. 8, 1916), 233 F. 861,* determined that a bankruptcy case ought to be reopened for the purpose of considering the status of a newly discovered trust interest; it expressly made no ruling as to the disposition of such interest. *In re Wright (C. C. A. 2, 1907), 157 F. 544,* holds that an insurance agent's contractural interest in renewal premiums is property within the meaning of the Bankruptcy Act, and *Fisher v. Cushman (C. C. A. 1, 1900), 103 F. 860,* is a similar holding with reference to an assignable liquor license.

It is believed, therefore, that the result reached in the Court of Appeals is not in accord with the weight of Federal authority.

CONCLUSION.

The petitioner and his counsel believe that the District Court's opinion correctly stated the Michigan law and correctly applied the Bankruptcy Act as construed by the great weight of Federal authority. The Circuit Court of Appeals should have affirmed the lower court. The bankruptcy practice in many states will be unsettled if the Circuit Court of Appeals is correct in its view of the relationship of the Bankruptcy Act and the widely-adopted state laws here in question. Opportunity for review is therefore requested.

Respectfully submitted,

RICHARD FORD,
Counsel for Petitioner.

MERLIN WILEY,
HOWARD STREETER,
LEON R. JONES,
Of Counsel.